



**COMMONWEALTH OF MASSACHUSETTS**  
**OFFICE OF CONSUMER AFFAIRS AND BUSINESS REGULATION**  
**DIVISION OF INSURANCE**

***REPORT OF EXAMINATION OF***  
**BLUE CROSS AND BLUE SHIELD OF MASSACHUSETTS HMO BLUE, INC.**

**Boston, Massachusetts**  
**As of December 31, 2015**

**NAIC GROUP CODE 3637**  
**NAIC COMPANY CODE 12219**  
**EMPLOYERS ID NUMBER 04-3362283**

BLUE CROSS AND BLUE SHIELD OF MASSACHUSETTS HMO BLUE, INC.

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**COMMONWEALTH OF MASSACHUSETTS**  
**Office of Consumer Affairs and Business Regulation**  
**DIVISION OF INSURANCE**

1000 Washington Street, Suite 810 • Boston, MA 02118-6200  
(617) 521-7794 • Toll-free (877) 563-4467  
<http://www.mass.gov/doi>

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GOVERNOR

**KARYN E. POLITO**  
LIEUTENANT GOVERNOR

**JAY ASH**  
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ECONOMIC DEVELOPMENT

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AND BUSINESS REGULATION

**GARY D. ANDERSON**  
ACTING COMMISSIONER OF INSURANCE

May 24, 2017

The Honorable Gary D. Anderson  
Acting Commissioner of Insurance  
Commonwealth of Massachusetts  
Division of Insurance  
1000 Washington Street, Suite 810  
Boston, MA 02118-6200

Honorable Commissioner:

Pursuant to your instructions and in accordance with Massachusetts General Laws, Chapter 176G, Section 10 and 211 CMR43, and other applicable statutes, an examination has been made of the financial condition and affairs of

**BLUE CROSS AND BLUE SHIELD OF MASSACHUSETTS HMO BLUE, INC.**

at its home office located at 101 Huntington Avenue, Suite 1300, Boston, MA 02199-7611. The following report thereon is respectfully submitted.

## **SCOPE OF EXAMINATION**

Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc. ("Company" or "HMO Blue") was last examined as of December 31, 2012 by the Massachusetts Division of Insurance ("Division"). The current examination was conducted by the Division and covers the three-year period from January 1, 2013 through December 31, 2015, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

The examination was conducted in accordance with standards and procedures established by the National Association of Insurance Commissioners ("NAIC") Financial Condition (E) Committee and prescribed by the current NAIC *Financial Condition Examiners Handbook*, the examination standards of the Division and with Massachusetts General Law. The Handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company, including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, as mentioned in the Massachusetts General Laws, Chapter 175, Section 4 and Chapter 176G, Section 10 and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Company.

The Company is audited annually by Ernst & Young ("EY"), an independent certified public accounting firm. The firm expressed unqualified opinions on the Company's financial statements for calendar years 2013 through 2015. A review and use of the Certified Public Accountants' work papers were made to the extent deemed appropriate and effective. The Company has an internal audit department. Work papers prepared by the Company's internal audit department have been reviewed as a source of information and were tested and leveraged as deemed appropriate and effective.

Representatives from the firm of KPMG LLP ("KPMG") were retained by the Division to assist in the examination by performing certain examination procedures at the direction of and under the overall management of the Division's examination staff. The assistance included a review of accounting records, information systems and investments. KPMG's Health Actuaries were involved in the performance of those procedures to the extent that such procedures related to the Company's reserves for unpaid claims and loss adjustment expenses and provider risk sharing settlements as of December 31, 2015.

KPMG's Information Technology Advisory Services personnel were engaged to review the adequacy and effectiveness of the Information Technology systems controls to determine the level of reliance to be placed on the information generated by the data processing systems.

### **SUMMARY OF SIGNIFICANT FINDINGS OF FACT**

There were no significant findings identified during the examination.

### **COMPANY HISTORY**

Blue Cross and Blue Shield of Massachusetts ("BCBSMA") began as the Associated Hospital Service Corporation of Massachusetts in 1937. The corporation aimed to spread the cost of hospital treatment among a large group of employed persons and, upon its opening, was the twenty-sixth plan of its kind in the United States, differing from others in its offering of statewide coverage. In 1939, the name Blue Cross was officially adopted by the American Hospital Association as the national symbol for the Hospital Service movement and in 1941, Blue Shield was established as a result of physician interest in the prepayment concept of financing health care.

Over the years, Blue Cross and Blue Shield of Massachusetts continued to grow and adapt to the needs of consumers, offering ever-increasing comprehensive coverage. The two separate organizations merged to become Blue Cross and Blue Shield of Massachusetts, Inc. and continued as part of a national network of affiliated plans, the Blue Cross and Blue Shield Association.

In January 2005, BCBSMA transferred its insured HMO business to a separately incorporated, not-for-profit subsidiary, Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc. ("HMO Blue"). HMO Blue provides hospitalization, medical and other health benefits as a licensed health maintenance organization. HMO Blue and BCBSMA operate under common management and Board of Directors ("Board") control. HMO Blue was licensed by the Division effective January 1, 2005. As a condition of granting an HMO license to HMO Blue, the Division required BCBSMA and HMO Blue to enter into an agreement to issue a surplus note to the other company if either entity's health risk based capital ("RBC") falls outside a specified range. BCBSMA also entered into a unilateral agreement with HMO Blue to guarantee all of HMO Blue's current and future financial obligations.

### **MANAGEMENT AND CONTROL**

#### **Board of Directors**

The minutes of meetings of the Board of Directors ("Board") and its Committees for the period under examination were read and they indicated that all meetings were held in accordance with the Company's bylaws and the laws of the Commonwealth of Massachusetts. Activities of the Committees were ratified at meetings of the Board.

## Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

HMO Blue and BCBSMA operate under common Board management and control. The bylaws specify that the business and affairs of the Company are controlled by a Board, the size of which is determined at each Annual Meeting of the members. Each director must be a member of the Company. Directors are elected at the Annual Meeting and serve for three years or until a successor is duly elected and qualified.

The Board shall meet annually immediately following the Annual Meeting of the members. Regular meetings shall be at such place and time as the Board may from time to time determine. The Annual Meeting of the directors is for the purpose of organization, election of the officers of the Company not elected by the members, establishment of committees of the directors and the transaction of such other business as may properly come before the meeting. Special meetings of the Board may be called on notice by the Secretary upon request by the Chair of the Board, the Chief Executive Officer or two or more directors.

At December 31, 2015, the Board was comprised of five directors, which was in compliance with Company bylaws. Directors duly elected and serving at December 31, 2015 are as follows:

### Director

### Title

Andrew C. Dreyfus  
Allen P. Maltz\*\*

President and Chief Executive Officer, BCBSMA  
Executive Vice President & Chief Financial Officer,  
BCBSMA

Bruce M. Bullen\*  
Stephanie S. Lovell

Chief Operating Officer, BCBSMA  
Executive Vice President, Medicare and Chief Legal  
Officer, BCBSMA

Phyllis R. Yale

Senior Advisor, Bain & Company, Inc.

\*Effective June 2016, Bruce M. Bullen resigned as a Director of BCBSMA. Mr. Bullen was replaced by Ms. Deborah Devaux.

\*\*Effective December 2016, Allen P. Maltz resigned as a Director of BCBSMA. Mr. Maltz was replaced by Ms. Andreana Santangelo.

### Officers

According to the Company's bylaws, the Board shall elect the officers of the Company. The officers of the Company are the chairman of the Board, the president and chief executive officer, chief operating officer, clerk, assistant clerk, executive vice president and treasurer, assistant treasurer, and chief actuary.

## Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

Officers of the Company at December 31, 2015 were as follows:

<u>Officer</u>	<u>Title</u>
Andrew C. Dreyfus	President & Chief Executive Officer
Bruce M. Bullen	Chief Operating Officer
Allen P. Maltz	Executive Vice President & Chief Financial Officer
Stephanie S. Lovell	Executive Vice President, Medicare and Chief Legal Officer & Clerk
Andreana Santangelo***	Chief Actuary
Phyllis R. Yale	Chair
Keith F. Renaldi	Treasurer
Alona G. Abalos	Assistant Clerk
Enrico A. Giammarco	Assistant Treasurer
Mark R. Collura	Assistant Treasurer

\*\*\* Effective December 2016, Andreana Santangelo replaced Allen Maltz as CFO

### Committees of the Board of Directors

The Board may delegate such of its powers as it considers advisable, except those powers which by law, the articles of organization, or the bylaws may not be so delegated, to such committees as the Board or the bylaws may from time to time establish. All committees shall serve at the pleasure of the Board. There are no current standing committees of the Board.

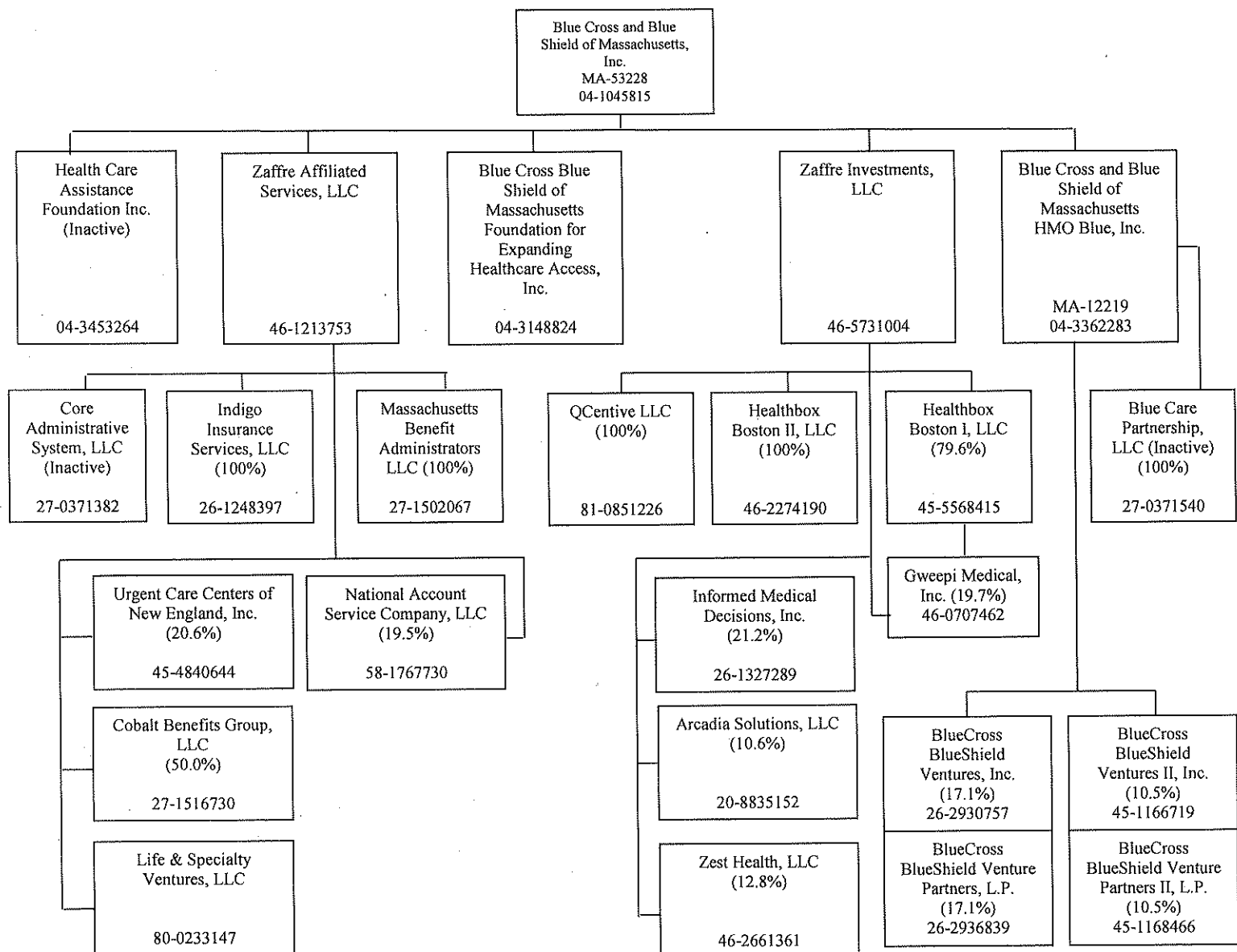
### Holding Company

As stated in the Insurance Holding Company System Form B and Form C as filed with the Division, the Company is a member of a holding company system and is subject to the registration requirements of Massachusetts General Law, Chapter 176G, Section 28 and Regulation 211 CMR 7.00. BCBSMA is the "ultimate controlling person" of the Holding Company System.

# Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

## Organization Chart

A summary of ownership and relationship of the Company and its operating subsidiaries and affiliated companies as of December 31, 2015 is illustrated below:



Transactions and Agreements with Subsidiaries and Affiliates

BCBSMA and HMO Blue operate under a common Board of Directors management and control. The Company participates in a bilateral inter-company agreement with BCBSMA to settle any claims, fees, administrative cost expense allocation, and pass-through cash and expenses paid by one company on behalf of the other company.

BCBSMA and HMO Blue have an inter-company loan agreement, which allows borrowings between the companies, however such amounts are limited to predetermined levels based on the certain financial measures.

HMO Blue also has one inactive wholly-owned subsidiary, Blue Care Partnership, LLC ("Blue Care Partnership"), and two affiliated companies, BlueCross BlueShield Venture Partners, L.P. ("BCBS Venture") and BlueCross BlueShield Venture Partners II, L.P. ("BCBS Venture II").

**TERRITORY AND PLAN OF OPERATION**

Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc. is headquartered in Boston, Massachusetts. The Company is licensed to transact business in the Commonwealth of Massachusetts. As of December 31, 2015, BCBSMA's service area included all of Massachusetts with a focus on the greater metropolitan Boston area.

During the course of the examination, a general review was made of the manner in which the Company conducts its business practices and fulfills its contractual obligations to members and claimants. This review was limited in nature and was substantially narrower than a full scope market conduct examination. No significant adverse practices were identified.

**REINSURANCE**

Since January 1, 2014, the Company has had health insurance premiums subject to the Affordable Care Act ("ACA") reinsurance program under the sharing provisions of the ACA. None of the Company's policies have been reinsured outside of the United States. None of the reinsurance agreements can be unilaterally cancelled except for nonpayment of premiums.

**FINANCIAL STATEMENTS**

The following financial statements have been prepared by management and filed by the Company with the Division and present the financial condition of the Company for the period ended December 31, 2015. These financial statements are the responsibility of Company management.

Statement of Assets, Liabilities, Surplus and Other Funds as of December 31, 2015

Statement of Income for the Year Ended December 31, 2015

Reconciliation of Capital and Surplus for Each Year in the Three Year Period Ended December 31, 2015

# Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

## Statement of Assets, Liabilities, Capital and Surplus as of December 31, 2015

	Per Annual Statement
<b>ASSETS</b>	
Bonds	\$ 824,490,516
Preferred stock	742,000
Common stock	243,780,360
Real estate properties occupied by the company	95,041,561
Cash, cash equivalents and short-term investments	47,661,879
Other invested assets	445,866,627
Receivables for securities	35,625,169
Subtotals, cash and invested assets	<u>1,693,208,112</u>
Investment income due and accrued	4,381,113
Premiums and considerations: Uncollected premiums and agents' balances	14,491,920
Premiums and considerations: Accrued retrospective premiums	79,476,630
Reinsurance: Amounts recoverable from reinsurers	25,209,585
Electronic data processing equipment and software	6,163,123
Receivables from parent, subsidiaries and affiliates	19,696,076
Healthcare and other amounts receivable	65,134,750
Aggregate write-ins for other than invested assets	350,276
Total Assets	<u>\$ 1,908,111,585</u>
<b>LIABILITIES</b>	
Claims unpaid	\$ 383,518,323
Accrued medical incentive pool and bonus amounts	77,927,330
Unpaid claims adjustment expense	4,640,871
Aggregate health policy reserves	19,312,087
Premiums received in advance	109,814,815
General expense due or accrued	22,497,327
Current federal and foreign income tax payable and interest	1,267
Borrowed money and interest thereon	167,650,514
Payable for securities	16,154,248
Aggregate write-ins for other liabilities	17,012,113
Total Liabilities	<u>818,528,895</u>
Aggregate write-ins for special surplus funds	40,550,000
Unassigned funds (surplus)	<u>1,049,032,690</u>
Total capital and surplus	<u>1,089,582,690</u>
Total liabilities, surplus and other funds	<u>\$ 1,908,111,585</u>

# Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

## Statement of Income For the Year Ended December 31, 2015

	Per Annual Statement
<b>Member Months</b>	<u>9,035,333</u>
Net premium income	\$ 4,354,485,059
Change in unearned premium reserves and reserve for rate credits	<u>3,635,523</u>
Total revenue	<u>4,358,120,582</u>
<b>Deductions:</b>	
Hospital/medical benefits	2,967,496,603
Other professional services	106,691,618
Emergency room and out-of-area	70,529,046
Prescription drugs	599,777,968
Incentive pool, withhold adjustments and bonus amounts	<u>166,780,705</u>
Subtotal	<u>3,911,275,940</u>
Net reinsurance recoveries	<u>(35,517,994)</u>
Total hospital and medical	<u>3,875,757,946</u>
Claims adjustment expense	181,237,777
General administrative expense	324,485,476
Total underwriting deductions	<u>4,381,481,199</u>
Net underwriting gain (or loss)	(23,360,617)
Net investment income earned	35,789,500
Net realized gains	<u>(10,727,558)</u>
Net investment gains	25,061,942
Aggregate write-ins for other income or expenses	<u>722,608</u>
Net income after capital gains tax and before other federal income taxes	<u>2,423,933</u>
Net income	<u>\$ 2,423,933</u>

Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

Reconciliation of Capital and Surplus  
For Each of the Three-Year Period Ended December 31, 2015

	2015	2014	2013
Capital and surplus, December 31, prior year	\$ 1,124,246,077	\$ 1,151,831,118	\$ 1,077,138,001
Net income	2,423,933	3,201,039	40,572,272
Change in net unrealized gains (losses)	(22,325,658)	(19,972,621)	26,471,911
Change in net deferred income tax			
Change in non-admitted assets	(14,761,662)	(10,813,459)	7,648,934
Net change in capital and surplus	(34,663,387)	(27,585,041)	74,693,117
Capital and surplus, December 31, current year	<u>\$ 1,089,582,690</u>	<u>\$ 1,124,246,077</u>	<u>\$ 1,151,831,118</u>

**ANALYSIS OF CHANGES IN FINANCIAL STATEMENTS RESULTING FROM THE  
EXAMINATION**

There have been no changes made to the financial statements as a result of the examination.

**COMMENTS ON FINANCIAL STATEMENT ITEMS**

As a result of the examination, no issues with non-compliance, adverse findings, or material changes to the financial statements were identified.

The Company uses estimates for determining its claims incurred but not yet reported which are based on historical claim payment patterns, healthcare trends and membership and includes a provision for adverse changes in claim frequency and severity. Amounts incurred related to prior years may vary from previously estimated liabilities as the claims are ultimately settled.

KPMG Health Actuaries prepared independent estimates of the Unpaid Claim Liabilities (“UCL”) as of December 31, 2015 and prior periods. For December 31, 2015, completion factors for the projection of ultimate claims were developed using historical payment patterns and actuarial judgment. “Low” and “High” estimates were developed by subtracting the claims paid-to-date from the actuarial range of incurred estimates. The actuarial estimates, as determined by KPMG Health Actuaries, indicate that HMO Blues’ UCL are reasonable as of December 31, 2015. The Company’s premium deficiency reserve calculation was reviewed and found to be reasonable as of December 31, 2015.

On January 1, 2014 HMO Blue became subject to an annual fee under section 9010 of the federal ACA. This annual fee was allocated to individual health insurers based on the ratio of the amount of the entity’s net premiums written to the amount of health insurance for any U.S. health risk that is written during the preceding calendar year.

A health insurance entity’s portion of the annual fee becomes payable once the entity provides health insurance for any U.S. health risk for each calendar year beginning on or after January 1 of the year the fee is due. As of December 31, 2015, the Company has written health insurance subject to ACA assessment, expects to conduct health insurance business in 2016, and estimates its portion of the annual health insurance industry fee payable on September 30, 2016, to be \$40,550,000. This amount is reflected in special surplus funds at December 31, 2015. Reporting the ACA assessment as of December 31, 2015, would impact RBC by (24.3%) and would not have triggered an RBC action level.

### **SUBSEQUENT EVENTS**

In December 2016, the Company issued a Surplus Note between BCBSMA HMO Blue and BCBSMA for \$100 million. The Surplus Note was issued to improve the RBC position of BCBSMA which resulted in an intercompany loan between the two entities. The Exam team notes that the Division of Insurance approved both the Surplus Note and the intercompany loan on December 8, 2016.

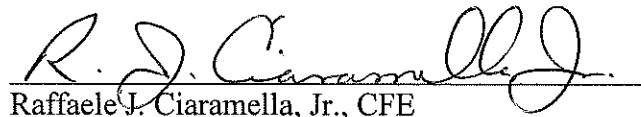
### **SUMMARY OF RECOMMENDATIONS**

There were no significant recommendations noted by the examination team for improvements in process, activities and/or controls that should be noted in this report.

**SIGNATURE PAGE**

Acknowledgement is made of the cooperation and courtesies extended by the officers and employees of the Company during the examination.

The assistance rendered by KPMG LLP who participated in this examination hereby is acknowledged.

A handwritten signature in cursive script, reading "R. J. Ciaramella, Jr.", written over a horizontal line.

Raffaele J. Ciaramella, Jr., CFE  
Supervising Examiner & Examiner-In-Charge  
Commonwealth of Massachusetts  
Division of Insurance